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SUBJECT: SCENESETTER FOR ADMINISTRATOR FORE'S VISIT TO KYIV

Summary

¶1. (SBU) Your November 22-23 visit to Kyiv will be an important sign of continuing USG support for international recognition of the Holodomor, the Great Famine of 1932-1933, which has been a top priority for President Yushchenko. Your visit will come at a time of an unfolding economic crisis and an ongoing struggle between President Yushchenko and Prime Minister Tymoshenko over whether to hold snap parliamentary elections. Political wrangling over election funding and other related legislation has delayed any election date until 2009, if early elections are held at all. Tymoshenko has rejected the necessity for new elections, citing the economic crisis. In early November the IMF approved a \$16.4 billion IMF package for Ukraine -- one of the largest in IMF history. A first tranche of \$4.5 billion was disbursed immediately after approval. At the time of this writing, the Rada is debating a second round of legislation aimed at meeting IMF requirements.

¶2. (SBU) Ukraine's relationship with Russia has remained tense following the Russia-Georgia conflict. President Yushchenko strongly supported President Saakashvili and issued decrees that seek to more closely regulate Russia's Crimea-based Black Sea Fleet (BSF). Yushchenko continues to push hard for NATO MAP. Senior officials have recently stated, however, that the main goal for the December NATO Ministerial will be signals (via MAP or other vehicles) that Ukraine is moving toward membership. End Summary.

Major Themes and Talking Points

¶3. (SBU) Your visit provides an opportunity to engage with key decision makers and underline our bilateral policy objectives. We suggest the following main themes:

- Holodomor: The U.S. strongly supports Ukraine's recognition of the tragedy of Holodomor. Both President Bush and Vice President Cheney paid homage at the Holodomor monument in Kyiv with Yushchenko this year.

- Financial: The President, Prime Minister, and Rada need to unite to deal with Ukraine's financial crisis. Providing examples of bipartisan approaches to the economic crisis in the U.S. could help underline this point.

- Energy: Ukraine needs to increase transparency in the energy sector, increasing competition, removing unnecessary middle-men (such as RosUkrEnergo), and establishing an open contracting system.

- NATO: At the NATO Summit in Bucharest in April, the Alliance committed to eventually extending membership to Ukraine. Ukraine must move forward on defense reform, economic reform and rule of law. We look forward to deepening our bilateral engagement with Ukraine to help advance its progress in these areas. There is no one set

path to NATO membership.

President Yushchenko Pushes Recognition of the Holodomor

¶4. (SBU) The "Holodomor," which means "death by hunger," is what Ukrainians call the 1932-33 Great Famine instigated by Stalin. President Yushchenko has taken a great personal interest in promoting commemoration of Holodomor and hopes that increased awareness of the famine will become an enduring part of his legacy. Ukrainian nationalists consider Holodomor a defining moment in Ukraine's history. The famine struck most heavily in what is now eastern Ukraine; it also struck parts of Russia and Kazakhstan. The famine was created after Ukrainian farmers resisted Soviet attempts to force peasants into collective farms. Soviet authorities confiscated the bulk of the food in the Ukrainian Socialist Soviet Republic to force the issue. Many scholars believe that 4-7 million deaths resulted from the famine; some Ukrainian politicians claim even greater losses.

¶5. (SBU) Ukraine is officially marking the Holodomor's 75th anniversary in 2008 with domestic and international events and is looking for as much outside recognition as possible. Ukraine passed a law in November 2006 declaring the Holodomor genocide against the Ukrainian people. The Government has sought recognition of the Holodomor as genocide in international fora. Russia is bitterly opposed to calling the Holodomor genocide. President Medvedev turned down an official invitation to attend the 75th anniversary events citing differences over the term genocide. The US has co-sponsored resolutions that do not include the genocide

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designation at UNESCO in October 2007, at the UNGA in 2003, and an OSCE statement in December 2007. The European Parliament passed a resolution recognizing the Holodomor as a crime against the Ukrainian people and humanity without referencing genocide in October 2008. The U.S. has told Ukraine that we are unable to support resolutions that call the Holodomor genocide. The United States supported the inclusion of an agenda item at the 63rd UNGA this year commemorating the 75th anniversary.

Orange Coalition Falters

¶6. (SBU) Orange Revolution allies Viktor Yushchenko and Yuliya Tymoshenko united forces following an unexpectedly strong showing by Tymoshenko's political bloc in the September 2007 pre-term parliamentary elections. They formed a coalition and established a government in late 2007 with Tymoshenko as Prime Minister, recreating their post-Orange Revolution alliance. Many hoped that they would work together better than they did in 2005, when Yushchenko dismissed Tymoshenko after seven months of infighting. Following an initial phase of cooperation, we again witnessed a string of mutual recriminations.

Two Headstrong Leaders

¶7. (SBU) President Yushchenko has a reputation as a visionary but critics say that his differences with Tymoshenko have prevented him from fulfilling the high expectations when he entered office in 2005. However, even his critics concede that his commitment to seeing Ukraine join NATO and the European Union is sincere. He has been relentless in pushing for Ukraine's request for a MAP. To Yushchenko, NATO membership is the only thing that can guarantee Ukrainian sovereignty and territorial integrity. He has stated that events in Georgia reinforce the need for collective security arrangements for Ukraine. Yushchenko has a close relationship with Georgian President Saakashvili, and is the godfather to Saakashvili's son. Significantly recovered from his 2004 dioxin poisoning, Yushchenko's

scarred face continues to clear up.

¶ 8. (SBU) Returning to political center stage after two years in opposition with her trademark braided hairstyle intact, PM Tymoshenko hit the ground running after her December 2007 confirmation as Prime Minister in a restored Orange coalition. She got a budget passed in eight days, completed her government program for the upcoming year, and made some progress in fulfilling campaign promises, such as to return lost savings from the defunct Soviet-era state savings bank. Tymoshenko joined Yushchenko and then Rada Speaker Yatsenyuk in signing a letter requesting a NATO Membership Action Plan (MAP) and spoke in favor of MAP during private meetings with the NATO SYG and North Atlantic Council during their June visit to Kyiv. Reflecting the public's ambivalence about NATO membership for Ukraine, Tymoshenko has avoided taking a public stance.

Elections Called, Date Uncertain

¶ 9. (SBU) On October 8, Yushchenko announced a decree disbanding the Rada and calling for pre-term parliamentary elections. In his address, Yushchenko once again blamed the Tymoshenko Bloc (BYuT) for the collapse of the coalition, pointing to BYuT's votes with Regions in the current Rada session. Without naming her, Yushchenko cast the blame on Tymoshenko, saying that he was "absolutely certain" that the democratic coalition was destroyed because of the "personal ambition of one person."

¶ 10. (SBU) PM Tymoshenko opposed the decision to call pre-term elections, citing the unfolding domestic economic crisis as requiring political continuity and stability. The call for elections, which require passage of laws both on administering and funding the vote, has thus far failed to find majority support in the Rada. There is still uncertainty on the date of the elections, or if they will be held at all.

Economic Challenges

¶ 11. (SBU) Ukraine's current financial crisis stems from a sharp decrease in international credit due to the global financial crisis and Ukraine's precarious balance of payments situation. Ukraine will have to finance \$50 to \$60 billion in foreign commitments due in 2009. Ukraine's banking sector, which grew rapidly in recent years thanks to

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aggressive foreign borrowing, is of chief concern. The main issue is the ability of banks to roll over short term external debt (currently totaling approximately \$13 billion) which will come due in the next few months. The current account deficit has ballooned in recent years and will total about \$13 billion this year. It will need to drop substantially next year if Ukraine is to meet its external commitments. Ukraine's foreign exchange reserves have dropped by 20% since the crisis began and totaled about \$31 billion in early November. The reserves will not cover all of the country's expected financing needs. Despite currency controls imposed by the National Bank, the hryvnia continues to show volatility.

Challenges to the Real Economy

¶ 12. (SBU) A downturn in global demand for steel and chemicals (Ukraine's chief exports), along with rising prices expected for gas imports and a downturn in credit conditions has led analysts to revise downward growth forecasts radically, with most now expecting zero or even negative real GDP growth in 2009, after about 7.4% growth in 2007 and about 4.5% this year. In addition to an unstable banking sector and an apparent contraction in the steel industry, we expect sharp

corrections in Ukraine's overheated construction and real estate sectors, an overall decline in investment, increased capital flight and rising energy prices.

Policy Responses to Financial Crisis

¶13. (SBU) The National Bank of Ukraine (NBU), pressed to stop a run on deposits in commercial banks, has sharply tightened capital controls in Ukraine's banking system, which has relied heavily on foreign borrowing to fuel its breakneck growth in recent years. The action comes after an estimated \$3 billion, or 4 percent of total deposits, were withdrawn from the banking system in mid to late October. Both the President and Prime Minister supported the IMF package that called for recapitalizing the banking sector and introducing stricter fiscal discipline, particularly as liberal public spending and public sector salary and pension policies have been a main cause of Ukraine's galloping inflation.

Ukraine and Energy

¶14. (SBU) The geopolitics and economics of energy continue to play a central role in Ukraine. Energy consumption per capita remains the highest in the world, and the energy infrastructure is decaying. Ukraine remains heavily dependent on gas and oil imports from Russia and Central Asia, and is the main transit country for Russian gas shipments to central and western Europe. Most Ukrainian policy-makers agree that Ukraine must diversify its sources of energy and move towards a market-based energy relationship with Russia, but Kyiv has yet to develop a long-term strategy to achieve these goals.

¶15. (SBU) The USG has encouraged Ukraine to open its energy market to more foreign investment. Few Ukrainian energy companies have the technical and financial resources to bring domestic production up to potential. Recent moves by the GOU to undercut its first-ever Production Sharing Agreement (PSA), signed with the U.S. company Vanco in 2007, are raising doubts about the GOU's sincerity in attracting foreign investment to develop domestic energy resources. There are some bright spots, however. Within the framework of the USG-supported Nuclear Fuels Qualification Project, Westinghouse has signed a contract to initially supply three Ukrainian reactors with fuel starting in 2011. This will help Ukraine diversify its sources of fuel for its nuclear power plants, all of which currently get their fuel from Russia. Russia also currently takes back spent nuclear fuel, but New Jersey-based Holtec has a contract to build a facility to store spent fuel within the country.

NATO/MAP

¶16. (SBU) The NATO Bucharest Summit did not grant a Membership Action Plan (MAP) to Ukraine. However, the Alliance declared that it sees Ukraine as a member in the future, urged intensified dialogue, and set a December 2008 date for an initial re-evaluation by Foreign Ministers. The Ukrainian government recently launched a NATO Public Information Campaign. Public opinion remains highly skeptical of the prospect of NATO membership, with less than 25 percent in favor and more than 50 percent opposed.

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¶17. (SBU) Following Russia's actions in Georgia, Ukraine requested emergency consultations with NATO allies to discuss threats to Ukraine's national security arising from that crisis. FM Ohryzko stated that events in Georgia argue strongly for even closer integration of Ukraine into the Euroatlantic community and for NATO membership. Yushchenko made a high-profile visit to Tbilisi on August 12 and, on the same day, signed two decrees meant to 1) regulate border

crossing for Russia's Black Sea Fleet (BSF) personnel, ships, and planes, and 2) require GOU permission for future BSF deployments. Yushchenko's move triggered a sharp exchange between Kyiv and Moscow. The MFA recently reconfirmed Ukraine's intention to hold Russia to the 2017 BSF withdrawal date agreed to in the 1997 basing agreement. The basing agreement requires either signatory to inform the other at least one year prior to the 2017 withdrawal deadline of its intention to enforce the agreement -- otherwise an automatic 5-year extension applies.

¶18. (SBU) Leading politicians from other parties have spoken of taking a less confrontational approach to the situation in Georgia. PM Tymoshenko has spoken of supporting the territorial integrity of Georgia, but warned of exacerbating regional tensions. She opposed Yushchenko's decrees to regulate the Black Sea Fleet as unenforceable and liable to further increase tensions with Russia. The Lytvyn Bloc, which advocates Ukrainian neutrality, released a statement urging Ukraine to give up its intentions to join NATO any time soon. The Party of Regions, headed by former PM Yanukovych, was critical of Yushchenko's support for Saakashvili and Ukraine's provision of arms to Georgia. Yanukovych spoke in favor of recognizing the "independence" of South Ossetia and Abkhazia.

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